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February 2, 2006

Mary L. Cottrell, Secretary
Department of Telecommunications and Energy
One South Station, 2nd Floor
Boston, Massachusetts 02110

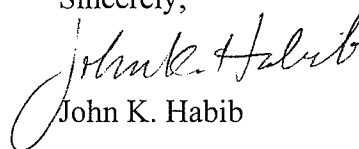
Re: Southern Union Company, D.T.E. 06-2

Dear Ms. Cottrell:

On behalf of Southern Union Company (the "Company"), please find enclosed the Company's Post Hearing Comments in this proceeding.

Please do not hesitate to contact me or Cheryl Kimball if we can provide you with any additional information concerning this matter.

Sincerely,



John K. Habib

Enclosures

cc: Andrew O. Kaplan, General Counsel
Jesse Reyes, Hearing Officer
Kevin Brannelly, Director, Rates and Revenue Requirements Division
George Yiankos, Director, Gas Division
Paul E. Osborne, Assistant Director, Rates & Revenue Requirements Division
Joseph Passaggio, Rates & Revenue Requirements
Glenn Shippee, Rates & Revenue Requirements
Joseph W. Rogers, Assistant Attorney General

COMMONWEALTH OF MASSACHUSETTS
DEPARTMENT OF TELECOMMUNICATIONS AND ENERGY

Southern Union Company

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D.T.E. 06-2

POST-HEARING COMMENTS OF SOUTHERN UNION COMPANY

I. INTRODUCTION

On January 9, 2006, Southern Union Company (“Southern Union” or the “Company”) filed a petition with the Department of Telecommunications and Energy (the “Department”) pursuant to G.L. c. 164, § 17A for approval and authorization to loan the proceeds of up to \$1.7 billion¹ in short-term bridge financing to its wholly owned subsidiary Southern Union Gathering Company LLC (“SUGC”) to complete its acquisition of Sid Richardson Energy Service, Ltd (“SRES”) and a related entity.² These funds will be used by SUGC to acquire SRES and to pledge its equity ownership in Panhandle Eastern Pipeline Company (“Panhandle Eastern”),³ as security for the interim bridge financing. Under G.L. c. 164, § 17A, Southern Union must obtain the Department’s authorization and approval in order to loan funds to SUGC and to pledge

¹ At this point, the Company assumes that its net financing needs are \$1.6 billion. However, the Company is seeking approval to loan “up to” \$1.7 billion to SUGC because the final price may change depending on the Net Working Capital Change Amount or out-of-pocket expenses, to be determined following the Closing Date (see, e.g., Exh. SU-2, § 2.5, at 12).

² On September 28, 2000, Southern Union, a Delaware corporation, acquired North Attleboro Gas Company and Fall River Gas Company, which now operate in Massachusetts subject to the Department’s jurisdiction under G.L.c. 164, § 1, under a d/b/a name “New England Gas Company”.

³ Panhandle Eastern Pipeline Company owns and operates 100 percent of a subsidiary company named Panhandle Eastern Pipe Line Company. The equity ownership being pledged in this transaction is that of the parent company.

its equity ownership in Panhandle Energy as collateral for the interim bridge financing to accomplish the transaction.⁴ The Department docketed the filing as D.T.E. 06-02.

Pursuant to notice duly issued, the Department conducted public and evidentiary hearings at its offices on January 27, 2006. There are no intervenors in this proceeding. In support of the petition, the Company offered the testimony of Richard N. Marshall, Vice President and Treasurer for Southern Union. The evidentiary record consists of 33 exhibits.

As discussed below, the record in this proceeding shows that the Company's proposal meets the Department's public-interest standard under G.L. c. 164, § 17A because the transaction will produce significant value for both customers and shareholders in terms of improving the overall financial position of the Company and creating the opportunity for the realization of financial and operational efficiencies. Accordingly, the Department should approve the Company's request as further described herein.

II. DESCRIPTION OF THE TRANSACTION AND SRES

SRES is a privately held natural gas gathering and processing company employing approximately 250 employees, led by a highly experienced senior management team and headquartered in Fort Worth, Texas (Exh. SU-1, at 4). SRES gathering and processing operations include: (i) field gathering and compression, (ii) treating, dehydration, sulfur recovery and other natural gas product conditioning, (iii) natural gas processing, and (iv) the sale of natural gas liquids and pipeline quality

⁴ As stated in the Purchase and Sale Agreement provided in Exhibit SU-2, Southern Union is required to close the transaction on or before March 1, 2006. Therefore, Southern Union is seeking to obtain the Department's approval (to the extent possible) prior to February 15, 2006.

residue gas (id.). The assets are commonly referred to as “midstream” natural gas assets (Tr. 1, at 6, 7). SRES has been a dependable provider of services to gas producers and suppliers in the Permian Basin for over 50 years (Exh. SU-1, at 4). SRES owns approximately 4,600 miles of natural gas and natural gas liquids pipelines in the Permian Basin, as well as four active cryogenic plants and six active natural gas treating plants (id.).

Following the acquisition, the SRES operations will be integrated with those of Southern Union, including Panhandle Eastern, which is headquartered in Houston, Texas (Exh. SU-1). As a result of the acquisition of SRES by SUGC and Southern Union Panhandle, Southern Union will operate an interstate distribution system through its subsidiaries comprised of approximately 22,000 miles of pipeline stretching from the Gulf of Mexico to the Southwest, Midwest and Canada and serving customers in 18 states (id.). The individuals at SRES who operate the business will be retained to maintain a continuity of expertise over the enterprise (Tr. 1, at 9).

Panhandle Eastern and SUGC will close the transaction with SRES using interim “bridge” financing (Exh. SU-1, at 6). As collateral for the interim bridge financing, the Company will pledge its ownership interest in Panhandle Eastern to the bridge loan lending parties (id.). The SUGC assets (acquired from SRES) will also serve as collateral for the bridge loan (id.). Upon acquisition, it is anticipated that there will be no debt outstanding at the SUGC level (id.). However, any debt incurred thereafter by SUGC for purposes of repaying the bridge loan or otherwise will be non-recourse to Southern Union and its utility operations (id.).

III. STANDARD OF REVIEW

G.L. c. 164, § 17A provides, in relevant part:

No gas or electric company shall, except in accordance with such rules and regulations as the [D]epartment shall from time to time prescribe, loan its funds to, guarantee or endorse the indebtedness of, or invest its funds in the stocks, bonds, certificates of participation or other securities of any corporation, association or trust unless said loan guaranty or endorsement, or investment is approved in writing by the [D]epartment.

G.L. c. 164, § 17A.

In Bay State Gas Company, D.P.U. 19886 (1979), the Department noted that no explicit standard of review is provided by § 17A, or in judicial or administrative construction of the statute. The Department, however, has recognized that the primary purpose of § 17A is to protect the ratepayers by assuring a utility's stable financial condition.⁵ In D.P.U. 19886, the Department also noted that "in keeping with the Supreme Judicial Court's interpretation of G.L. c. 164, § 14, we believe that implicit in the statutory framework in which § 17A is found is that a proposed investment must be consistent with the public interest."

In Boston Edison Company, D.P.U. 850 (1983), the Department further defined the parameters of a § 17A proposal, which is "consistent with the public interest:"

The General Court did not, in our view, intend that proposals be held "inconsistent" with the public interest merely because a fair assessment of the relevant factors recognizes that both beneficial and negative aspects may attend those proposals. Consequently, even if a particular proposal has negative aspects, we will find that such a proposal is consistent with the public interest if, upon consideration of all its significant aspects viewed as a whole, the public interest is at least as well served by approval of the proposal as by its denial.

⁵ Commonwealth of Mass., Dept. of Pub. Util., Recommendations of the Department of Public Utilities to the General Court at 2, House Doc. No. 53 (1954); see also E. Gadsby, 1 Annual Survey of Massachusetts Law at 182 (1954).

In Bay State Gas Company, D.P.U. 91-165 (1992), the Department reaffirmed the standard of review articulated in D.P.U. 850, that proposals filed under § 17A must be consistent with the public interest, and that they meet this standard if, upon consideration of all of the significant aspects of a proposal, the public is at least as well served by approval of the proposal as by its denial. In D.P.U. 91-165, at 7, the Department further noted that the application of the consistency standard in a § 17A case is based on the totality of what can be achieved by the proposal rather than a determination of any single gain which might be derived from the proposed transactions.

The Department also found that the consistency standard best accommodates the Department's interest in protecting the utility's ratepayers from the adverse effects of unwarranted § 17A transactions and a utility's interest in having flexibility in a changing marketplace to meet long-term objectives of its ratepayers and shareholders. D.P.U. 91-165, at 7. In D.P.U. 91-165, the Department articulated some of the factors that should be considered in evaluating § 17A petitions. These include: the nature and complexity of the proposal, the relationship of the parties involved in the underlying transaction, the use of the funds associated with the proposal, the risks and uncertainties associated with the proposal, the extent of the regulatory oversight on the parties involved in the underlying transaction, and the existence of safeguards to ensure the financial stability of the utility. After consideration of such a petition, viewed as a whole in light of the described factors, the Department may approve a § 17A investment if it finds the investment is consistent with the public interest.

IV. THE COMPANY'S PROPOSAL MEETS AND EXCEEDS THE DEPARTMENT'S STANDARD OF REVIEW UNDER G.L. c. 164, § 17A.

In determining whether an investment is in the public interest for purposes of § 17A, the Department considers the overall anticipated effect on customers of the potential benefits and harms of the proposal. Southern Union Company, D.T.E. 04-75, at 7 (2004); Southern Union Company, D.T.E. 03-3, at 14 (2003); Massachusetts Electric Company, D.T.E. 01-104, at 4 (2002), citing Bay State Gas Company, D.P.U. 91-165, at 7 (1992); Boston Edison Company, D.P.U. 850 (1983).

The Company's investment in SRES has several potential benefits for the Company's Massachusetts customers. First, the addition of the SRES operations is expected to enhance the financial operations of the Company, which would benefit the customers of the Company's distribution companies in terms of access to capital markets and the Company's cost of capital (Exh. SU-1, at 8). Specifically, the Company's financial analysis shows that the acquisition of the SRES operations will generate significant earnings, free cash flow and potential financial and operating synergies that will appreciably strengthen the Company's financial position (Exh. DTE -1 -10).

With respect to earnings, based on the Company's current research and assessment of various operational and financial considerations, the Company expects SRES to produce gross margin of approximately \$290 million, net earnings before interest, taxes, depreciation and amortization of approximately \$230 million, and net earnings of approximately \$70 million (*id.*). These enhanced earnings will make the Company more attractive to investors and has the potential to result in a reduction in the Company's cost of capital.

The yield of “free cash flow” (which is defined as net income plus depreciation less maintenance capital requirements) is expected to be in excess of 20 percent annually, more than twice the current yield of the Company’s existing business segments (Exh. DTE-1-10). The Company expects this significant free cash flow generation to be used to quickly reduce debt and further enhance its capital position (id.). Likewise, on January 27, 2006, the Company announced that it will be selling its Pennsylvania local distribution company (“LDC”) operations for \$580 million (Tr. 1, at 5). These proceeds also will be used to repay borrowings on the bridge facility, once it closes (id. at 12). Ultimately, increased free cash flow and proceeds from the sale of the Company’s Pennsylvania LDC will benefit customers in terms of the Company’s ability to attract capital at optimal rates, to maintain cash flows, to maintain stable rates and to provide a high level of customer service (id.; see also Tr. 1, at 8).

Moreover, as a result of the addition of the SRES operations, Southern Union will have the opportunity to achieve financial and operating synergies that will help to control and/or reduce costs for the overall system (Exh. SU-1, at 7). These potential synergies would not be available to customers in the absence of the SRES arrangement (id.).

For example, based on its experience with the Panhandle Eastern and CrossCountry Energy LLC transactions, the Company expects that its Massachusetts division will benefit from projected operating synergies that will reduce corporate overhead allocations through the Company’s Joint and Common Cost allocation model (Exh. DTE-1-07). Specifically, with the addition of the SRES operations, the Company expects that it will be able to allocate its fixed corporate governance and management costs over a larger asset base, which will allow each business unit of the Company to

incur a proportionately lower share of expenses (id.; Exh. DTE-1-18). The types of costs allocated among the operating units are those that are incurred to provide services at the corporate level necessary to the operation of a public company, including treasury operations, accounting operations, insurance, information technology services and purchasing (Exh. DTE-1-07; Exh. DTE-1-18).

Furthermore, with the addition of the SRES operations, the Company will have greater purchasing power in relation to materials or other items that may be used throughout the Company's operations and with that purchasing power, the Company can obtain greater discounts that are then passed on throughout the company (Exh. DTE-1-07). As a result, Southern Union will be better positioned to continue to maintain stable rates for Massachusetts customers on a going-forward basis.

Likewise, for several reasons, the integration of the SRES operations into Southern Union's operations would have no negative effect on the Company's ability to manage its local gas distribution activities (Exh. SU-1, at 7). Southern Union's due diligence efforts in connection with the acquisition showed no regulatory, legal or environmental issues that would have a material impact on the performance or operation of the SRES assets (id.). The SRES facilities have a well-established track record of safe and reliable operation (id.). In addition, Southern Union will manage the activities of SRES as a subsidiary with designated personnel and resources just as it has been operating Panhandle Eastern and CrossCountry, which have had no negative impact on the local distribution activities of the Company (id.). Lastly, SRES has a highly experienced senior management team, all of who are expected to be retained post-

acquisition (id.; Tr. 1, at 9). For these reasons, customers bear no risk and can only benefit from the proposed investment

As noted above, the Department has determined that, under G.L. c. 164, § 17A, a petitioner must demonstrate that its proposal is consistent with the public interest and that a petitioner would meet this standard if, upon consideration of all of the significant aspects of a proposal, the public is at least as well served by approval of the proposal as by its denial. See Bay State Gas Company, D.P.U. 91-165 (1992). The Department has further noted that the application of the public-interest standard in a Section 17A case is based on the totality of what can be achieved by the proposal rather than a determination of any single gain (or loss) that might be derived from the proposed transactions. Id.

In this case, the record shows that, after balancing all of the factors involved, the investment will have no negative effect on the service provided, or rates charged, to customers of the New England Gas Company, and therefore, meets the Department's no net harm public-interest standard. Customers will be at least as well served by the Department's approval of the proposed investment as by its denial. Therefore, the Department should grant the Company's request for approval under G.L. c. 164, s. 17A.

V. CONCLUSION

The record in this proceeding shows that proposed loan of up to \$1.7 billion by the Company to SUGC for purposes of allowing SUGC to complete its acquisition of SRES is in the public interest, as required by G.L. c. 164, § 17A. Therefore, for the reasons stated above, the Department should:

VOTE: That approval and authorization pursuant to G.L. c. 164, § 17A to loan the proceeds of a short-term bridge loan to Southern Union Gathering

Company LLC to fund the acquisition of SRES, is in the public interest as required by G.L. c. 164, § 17A.

VOTE: That approval and authorization pursuant to G.L. c. 164, § 17A to pledge Southern Union's equity ownership in Panhandle Eastern Pipe Line Company, is in the public interest as required by G.L. c. 164, § 17A.

ORDER: That the Department approves and authorizes Southern Union to loan the proceeds of a short-term bridge loan to Southern Union Gathering Company LLC to fund the acquisition of SRES, in conformity with all the provisions of law relating thereto.

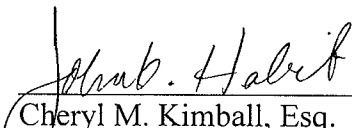
ORDER: That the Department approves and authorizes Southern Union to pledge its equity ownership in Panhandle Eastern Pipe Line Company, in conformity with all the provisions of law relating thereto.

ORDER: Such other and further orders and approvals as may be necessary or appropriate.

Respectfully submitted,

SOUTHERN UNION COMPANY

By its attorneys,


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Dated: February 2, 2006